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ZNR UUUUU ZZH
R 061549Z DEC 07
FM AMEMBASSY LUXEMBOURG
TO RUEHC/SECSTATE WASHDC 6154
INFO RUCNMEM/EU MEMBER STATES
RUCPDOC/DEPT OF COMMERCE WASHDC
RUEATRS/DEPT OF TREASURY WASHDC

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TREASURY FOR ATUKORALA

E.O. 12958: N/A
TAGS: EFIN EINV PGOV EU LU
SUBJECT: LUXEMBOURG HOLDS OFF PROPOSED VAT CHANGES

REF: LUXEMBOURG 235

¶1. SUMMARY. At the 4 December Ecofin meeting, Luxembourg won crucial concessions from other EU member states on a proposal to change how the value-added tax (VAT) on services is levied and protected its comparative VAT advantage as well as a vital revenue source. These proposed changes would have eliminated a GOL-estimated 220-270 million EUR yearly in tax revenues. The concessions gained preserve for Luxembourg the current VAT collection arrangement through 2014. There will then be an extended phase in period over the course of 5 years. This decision is very good news for the GOL and protects what PM Juncker has estimated to be nearly 1% of Luxembourg's GDP. It is also good news for American e-commerce companies established in Luxembourg. END SUMMARY.

¶2. Luxembourg lifted its "veto" at the 4 December EU Economic and Finance (Ecofin) ministers' meeting clearing the way for sweeping changes regarding how VAT is levied on services in the EU. It lifted its veto only after it gained key concessions on the proposal from other Member States. Whereas previous proposals either went into effect immediately or only allowed Luxembourg to keep reduced amounts of VAT collected (Reftel), Luxembourg was able to extract concessions which fended off any practical changes until 2014. Thereafter there would be a phase-in period where Luxembourg would retain 30% of the VAT receipts for 2015-2016, and then 15% for the period 2017-2018. The changes would come into full effect on 1 January 2019.

¶3. An economic advisor to PM (and Finance Minister) Juncker told Pol/Econ Chief that that the GOL was "delighted" with the outcome and said Juncker's high standing among fellow EU finance ministers was absolutely pivotal in winning the concessions. He also said that these concessions establish the "formal legal framework" that e-commerce companies established or considering establishing themselves in Luxembourg need to plan for the next decade.

¶4. In comments to Parliament on 5 December, Juncker himself credited the efforts of Luxembourgish civil servants working "in the background." He further described the compromise as a "typical European compromise," containing "no special treatment for Luxembourg." Juncker said that Luxembourg was doing nothing illegal by establishing a 15% VAT rate and pointed out that every other Member State could avail themselves of this same low rate if they so desired. He said that this compromise was very important to the Luxembourg e-commerce sector and predicted that over the next eight years (before the changes go into effect); Luxembourg would continue to attract new companies. More importantly, he predicted they would stay beyond 2015 "for other reasons." Those Juncker cited were stability, location, labor market,

and quality of services found in Luxembourg.

¶5. COMMENT: The crux of the issue for Luxembourg regards how VAT on services specifically effects the Luxembourg e-commerce sector. For several years, the GOL has actively marketed its advantage vis-a-vis VAT to e-commerce companies. Many, almost exclusively U.S. companies, have established themselves in Luxembourg as a result. The GOL has worked hard to diversify its economy from financial services on which it relies for the vast majority of its GDP (more than 30% of Luxembourg's GDP comes from the finacial services sector). It has been extremely proud of its record in this campaign, luring heavyweights such as iTunes, Skype, and PayPal to Luxembourg. This agreement represents a near-best case outcome for the GOL. It has forged an EU consensus, preserved its comparative VAT advantage for the near-term, and protected a significant source of revenue. END COMMENT
WAGNER